

TAIWAN

The Department of State submitted this report to the Senate Committees on Foreign Relations and on Finance and to the House Committees on Foreign Affairs and on Ways and Means, on January 31, 1999.

Key Economic Indicators
(Billions of U.S. Dollars unless otherwise noted)

	1996	1997	1998	1/
<i>Income, Production and Employment:</i>				
GDP (at current prices)	272.3	283.3	260.9	
Real GDP Growth (percent)	5.7	6.8	5.3	
GDP by Sector:				
Agriculture	8.9	7.7	6.7	
Manufacturing	76.0	78.4	72.5	
Services	144.6	155.8	145.0	
Government	28.7	29.5	26.5	
Per Capita GDP (US\$)	12,732	13,130	11,976	
Labor Force (000s)	9,310	9,432	9,555	
Unemployment Rate (percent)	2.6	2.7	2.6	
<i>Money and Prices (annual percentage growth):</i>				
Money Supply (M2)	9.1	8.0	8.3	
Consumer Price Inflation	3.1	0.9	1.9	
Exchange Rate (NT\$/US\$) 2/				
Official	27.46	28.95	33.30	
<i>Balance of Payments and Trade: 3/</i>				
Total Exports FOB 4/	115.9	122.1	111.5	
Exports to U.S. CV 5/	29.9	32.6	33.5	
Total Imports CIF 4/	102.4	114.4	106.7	
Imports from U.S. FAS 5/	18.4	20.4	17.7	
Trade Balance 4/	13.5	7.7	4.8	
Trade Balance with U.S. 5/	11.5	12.2	15.8	
External Public Debt	0.1	0.1	.05	
Fiscal Deficit/GDP (pct)	7.4	6.3	5.0	
Current Account Surplus/GDP (pct)	4.0	2.7	2.3	
Debt Service Payments/GDP (pct)	0.7	0.7	0.7	
Gold and Foreign Exchange Reserves	93.6	88.2	90.0	
Aid from U.S. 6/	0	0	0	

Aid from Other Countries	0	0	0
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1/ 1998 figures are estimated based on data from the Directorate General of Budget, Accounting and Statistics, or extrapolated from data available as of September 1998.

2/ Average of figures at the end of each month.

3/ Merchandise trade.

4/ Taiwan Ministry of Finance (MOF) figures for merchandise trade.

5/ Sources: U.S. Department of Commerce and U.S. Census Bureau; exports FAS, imports customs basis; 1998 figures are estimates based on data available through August. Taiwan MOF figures for merchandise exports (FOB) to and imports (CIF) from the U.S. were (US\$ billions): (1996) 26.9/20.0, (1997) 29.5/23.2, (1998) 30.0/19.3.

6/ Aid disbursements stopped in 1965.

1. General Policy Framework

For four and a half decades, Taiwan has maintained rapid growth and macroeconomic stability. Annual economic growth during this period averaged 8.5 percent. In 1997, real Gross Domestic Product (GDP) increased 6.8 percent. However, financial turmoil in East Asia slowed the growth rate to about 5 percent in 1998. Per capita GDP was \$13,130 in 1997. The per capita GDP estimate for 1998 is \$11,976. This decline is due to the depreciation of the New Taiwan Dollar. As of September 1998, Taiwan held \$84 billion in foreign exchange reserves, the third largest in the world (after Japan and the PRC). Prices rose one percent in 1997 and are expected to rise two percent in 1998.

Rising labor and land costs have long led many manufacturers in labor intensive industries to move offshore, mainly to Southeast Asia and mainland China. Industrial growth is now concentrated in capital and technology intensive industries such as petrochemicals, computers, semiconductors, and electronic components, as well as consumer goods industries. Services account for 55.6 percent of GDP. Merchandise exports accounted for 44 percent of GDP in 1998.

Falling official savings and growing public expenditure have caused domestic public debt to increase steadily. The Taiwan authorities now rely largely on domestic bonds and bank loans to finance major expenditures. Taiwan has adopted austerity measures to control the government budget deficit in recent years. As a result, outstanding public debt, which declined from 21 percent of GNP in 1997 to 19.4 percent in 1998, will drop further to 17 percent in 1999 and 15 percent in 2000 (all data on a fiscal year basis, July 1-June 30). The central government's deficit will fall from four percent of GDP in 1997 to one percent in 2000. Defense spending still accounts for the largest share of public expenditures (about one quarter), but is falling in relative terms. The greatest pressure on the budget now comes from growing demands for improved infrastructure and social welfare spending, including a national health insurance plan initiated in early 1995.

Taiwan wishes to accede to the World Trade Organization (WTO) in the near future. As part of the accession process, Taiwan and the United States signed a landmark bilateral WTO agreement in February, 1998. The agreement includes both immediate market access and phased-in commitments, and will provide substantially increased access for U.S. goods, services, and agricultural exports to Taiwan. Taiwan is also an active member of the Asia Pacific Economic Cooperation (APEC) forum.

2. Exchange Rate Policies

Taiwan has a floating exchange rate system in which banks set rates independently. The Taiwan authorities, however, control the largest banks authorized to deal in foreign exchange. The Central Bank of China (CBC) intervenes in the foreign exchange market when it feels that

speculation or "drastic fluctuations" in the exchange rate may impair normal market adjustments. The CBC uses direct foreign exchange trading by its surrogate banks and public policy statements as its main tools to influence exchange rates. The CBC still limits the use of derivative products denominated in New Taiwan Dollars (NTD).

Trade-related funds flow freely into and out of Taiwan. Most restrictions on capital account flows have been removed since late 1995. Laws restricting repatriation of principal and earnings from direct investment have been lifted. Despite significant easing of previous restrictions on foreign portfolio investment, some limits remain in place.

3. Structural Policies

Fifteen state-owned enterprises have been either totally or partially privatized in the past three years. Nine more are targeted for privatization in 1999. State-owned enterprises account for 9.5 percent of GDP, a proportion which shrinks annually. Taiwan's Fair Trade Commission (FTC) acts to thwart noncompetitive pricing by state-run monopolies. FTC exemptions granted five years ago to several state-run monopolies were not renewed in 1997, making such firms subject to anti-monopoly laws.

Taiwan has been lowering tariffs significantly in recent years. In May, 1998, Taiwan began implementing tariff cuts on 1,130 items, many of specific interest to U.S. industry. In 1998, authorities also enacted tariff cuts on 245 high-tech products under the Information Technology Agreement. Tariff reductions on 15 agricultural products, negotiated during the U.S.-Taiwan bilateral WTO accession negotiations, took effect in July 1998. An additional 777 items are slated for tariff cuts shortly. Taiwan's current average nominal tariff rate is 8.3 percent; the trade-weighted rate is 3.2 percent.

High tariffs and pricing structures on some goods -- in particular on some agricultural products -- nevertheless hamper U.S. exports. However, under the bilateral WTO agreement reached in February, Taiwan began to provide quotas for the importation of previously-banned pork, poultry, and variety meat products. The Taiwan Tobacco and Wine Monopoly Bureau (TTWMB) has a monopoly on domestic production of cigarettes and alcoholic beverages. As part of its bilateral WTO commitments to the United States, however, Taiwan has pledged to convert an existing monopoly tax on these products to a simpler tax and tariff-based system, and also to open these markets following the passage and implementation of new legislation now pending in the Legislative Yuan.

4. Debt Management Policies

Unofficial estimates put Taiwan's outstanding long and short-term external debt at \$20 billion as of December 1997, equivalent to seven percent of GDP. Official figures show Taiwan's long term outstanding external public debt totaled \$64 million as of June 1998, compared to gold

and foreign exchange reserves of about \$88 billion. Taiwan's debt service payments in 1997 totaled \$2.1 billion, only 1.5 percent of exports of goods and services.

Foreign loans committed by Taiwan authorities exceed \$3.6 billion. Taiwan offered low-interest loans to the Philippines, Eastern Europe, Vietnam, South Africa, and Latin America, mostly to build industrial zones and to foster development of small and medium enterprises. Some of the loans were provided to several Southeast Asian nations to address financial crises. Taiwan also contributes to the Asian Development Bank (ADB), one of the two multilateral development banks in which it has membership. Taiwan is also a member of the Central American Bank for Economic Integration (CABEI). The ADB, CABEI, the European Bank for Reconstruction and Development (EBRD) and a number of other international organizations have all floated bonds in Taiwan.

5. Significant Barriers to U.S. Exports

Accession to the WTO agreement by Taiwan will open markets for many U.S. goods and services. Of some 10,200 official import product categories, nearly 86 percent are completely exempt from any controls. 991 categories are still “regulated” and require approval from relevant authorities based on the qualifications of the importer, the origin of the good, or other factors. Another 279 require import permits from the Board of Foreign Trade or pro forma notarization by banks. Imports of 270 categories are “restricted,” including ammunition and some agricultural products. These items can only be imported under special circumstances, and are thus effectively banned.

Financial: Taiwan continues to steadily liberalize its financial sector. Taiwan enacted a Futures Exchange Law in March 1997; a futures market was established in July 1998. The Securities and Exchange Law was amended in May 1997 to remove restrictions on employment of foreigners by securities firms, effective upon Taiwan's accession to the WTO. Limits remain on foreign ownership in listed companies. For qualified foreign institutional investors, restrictions on capital flows have been removed, although they are still subject to limits on portfolio investment. Foreign individual investors are subject to some limits on their portfolio investment and restrictions on their capital flows.

Banking: In June 1997, the annual limit on a company's trade-related outward (or inward) remittances was raised from \$20 million to \$50 million. Inward/outward remittances unrelated to trade by individuals or companies are still subject to annual limits. NTD-related derivative contracts may not exceed one-third of a bank's foreign exchange position. To stabilize the foreign exchange market in the wake of regional financial turmoil, the CBC closed the non-deliverable forward (NDF) market to domestic corporations in May 1998; the NDF market remains open to foreign companies.

Legal: Foreign lawyers may not operate legal practices in Taiwan but may set up consulting firms or work with local law firms. Qualified foreign attorneys may, as consultants to

Taiwan law firms, provide legal advice to their employers only. Legislation was passed in May to clarify the status and scope of work for foreign-licensed attorneys, and also to permit the eventual establishment of foreign legal partnerships. However, last minute changes to the law failed to achieve this purpose, and may be inconsistent with Taiwan's WTO commitments. Taiwan authorities have pledged to remedy these inconsistencies and for now the new law is not being implemented.

Insurance: In May 1997, the financial authorities announced that in principle insurance companies would be allowed to set some premium rates and policy clauses without prior approval from regulators. Insurance companies are still required to report such rates and clauses. In July 1995, Taiwan removed a prohibition against mutual insurance companies; as of late 1998, however, authorities had not issued implementing regulations.

Transportation: The United States and Taiwan concluded an Open Skies Agreement in February 1997. An amendment to the Highway Law allowing branches of U.S. ocean and air freight carriers to truck containers and cargo in Taiwan went into effect on November 1, 1997.

Telecommunications: Taiwan opened its mobile phone market to full competition in 1997. Fixed line services remain monopolized by Chunghwa Telecom, a state-owned corporation. Taiwan plans to issue a limited number of new fixed line licenses in 1999 to provide competition for Chunghwa. Under its WTO services schedule, it is committed to full market opening by July, 2001. Under the bilateral WTO agreement signed in February, Chunghwa began in October to lower excessively high interconnection fees previously imposed on mobile service providers. Taiwan also agreed to raise the current 20 percent limit on foreign ownership of a telecom firm to 60 percent through a combination of direct and indirect ownership. This change, however, is unlikely to be enacted until mid-1999 at the earliest.

Pharmaceuticals and Medical Devices: Taiwan's single payer socialized health care system discriminates against imported drugs by setting prices for leading brand-name products at artificially low levels, while providing artificially high reimbursement prices for locally-made generics. The process by which Taiwan registers and prices new drugs is also time-consuming and cumbersome. In 1998, however, Taiwan authorities began a two-year phase-out of a burdensome requirement for clinical trials as part of the registration process for new drugs. High value-added imported medical devices are likewise put at a competitive disadvantage by Taiwan's reimbursement system, which fails to account for significant quality differences between different brands of medical devices.

Movies and Cable TV: Taiwan eased import restrictions on foreign film prints from 38 to 58 per title in late 1997. The number of theaters in any municipality allowed to show the same foreign film simultaneously also increased from 11 to 18. Effective August 1997, multi-screen theaters are allowed to show a film on up to three screens simultaneously, up from the previous limit of one. Taiwan has pledged to abolish these restrictions upon accession to the WTO. In the cable TV market, concerns are growing that the island's two dominant Multi-System

Operators (MSOs) are colluding to inhibit fair competition. Control by the two MSOs of upstream program distribution is making it increasingly difficult for U.S. providers of popular channels to negotiate reasonable fees for their programs.

Standards, Testing, Labeling, and Certification: Taiwan will bring its laws and practices into conformity with the WTO Agreement on Technical Barriers to Trade as part of its WTO accession. U.S. agricultural exports in particular suffer under existing requirements. These include a lack of an internationally-accepted set of pesticide tolerance levels for imported fruits and vegetables, stringent chemical testing of imported food products, and standards on preservatives for soft drinks. Imported agricultural goods are routinely tested while local agricultural products usually are not. Industrial products such as air conditioning and refrigeration equipment, electric hand tools, and synthetic rubber gloves must undergo redundant and unnecessary testing requirements, which include destructive testing of samples. Imported autos face stringent noise emissions and fuel efficiency testing requirements. In 1997, Taiwan authorities promulgated new Electromagnetic Compatibility (EMC) standards for computer and other electronic goods. In October, 1998, the U.S. and Taiwan initialed an agreement under which Taiwan will recognize EMC testing performed by accredited U.S. labs. Final implementation awaits approval by Taiwan's Cabinet.

Investment Barriers: Taiwan continues to relax investment restrictions in a host of areas, but foreign investment remains prohibited in key industries such as agriculture, basic wire line telecommunications, broadcasting, and liquor and cigarette production. Wire line telecommunications will be gradually liberalized beginning in 1999, and will be completely liberalized by July, 2001 under Taiwan's WTO commitments. Liquor and cigarette production will be fully liberalized by 2004.

Limits on foreign equity participation in a number of industries were relaxed in 1997; for example, permissible participation in shipping companies was raised from 50 to 100 percent. A 33 percent limit on holdings in air cargo forwarders and air cargo ground-handling was raised to 50 percent in 1998, but remains unchanged for airlines. However, an amendment to the Civil Aviation Law that would raise the holding limit to 50 percent is now pending legislative approval. In August 1997, Taiwan raised the cap on foreign investment in independent power projects from 30 percent to 49 percent. Local content requirements in the automobile and motorcycle industries will be lifted as part of Taiwan's WTO accession. Restrictions on employment of foreign administrative personnel in foreign-invested firms remain in place.

Procurement Practices: Taiwan has committed to adhere to the WTO Agreement on Government Procurement (AGP) as part of its WTO accession. To prepare for this commitment, a new Government Procurement Law was passed and promulgated in mid-1998, marking an important step towards open, fair competition in Taiwan's multi-billion dollar market for public procurement projects. The new law is being implemented and enforced by a reorganized body, the Government Procurement and Public Construction Commission.

6. Export Subsidies Policies

Taiwan provides an array of direct and indirect subsidy programs to farmers, ranging from financial assistance to guaranteed purchase prices higher than world prices. It also provides incentives to industrial firms in export processing zones and to firms in designated "emerging industries." Some of these programs may have the effect of subsidizing exports. Taiwan is currently in the process of notifying the WTO of these programs, and as part of its WTO accession, it may be required to amend or abolish any subsidy programs deemed inconsistent with WTO principles.

7. Protection of U.S. Intellectual Property

Taiwan is not a party to any major multilateral IPR conventions. In line with WTO accession efforts, Taiwan has passed laws to protect integrated circuit layouts, personal data, and trade secrets. Taiwan currently protects copyrights dating from 1965. Revised Copyright, Patent, and Trademark Laws were passed in 1997. However, only the Trademark Law and certain provisions of the Copyright Law have been implemented. The new Copyright Law, which will be fully implemented only upon WTO accession, will extend retroactive copyright protection to 50 years. Taiwan implemented these changes to bring its IPR legal structure into conformity with the WTO TRIPs agreement.

Citing persistent enforcement problems, the United States put Taiwan back on the Special 301 Watch List in August, 1998. The U.S. is particularly concerned about inadequate enforcement efforts in the face of continued production and export of counterfeit U.S. software and video games to the U.S. and third countries. In 1997, Taiwan was the second largest source of counterfeit goods seized by U.S. Customs. Another key enforcement weakness in the existing system is the unwillingness of some judges and prosecutors to accept foreign-issued powers of attorney in IPR prosecutions. Taiwan authorities are presently taking steps to address these and other enforcement issues.

8. Worker Rights

a. The Right of Association: Although the right to organize was reaffirmed by Taiwan's Judicial Yuan in 1995 as a constitutional right, the Labor Union Law (LUL) forbids civil servants, teachers, and defense industry workers from organizing trade unions and forbids workers from forming competing trade unions and confederations. However, as democratization has continued, workers have gradually established independent labor organizations, either legally or illegally, and these independent unions are increasingly challenging the leadership of the Chinese Federation of Labor. As of June 1998, 2.9 million workers, or 31 percent of Taiwan's labor force, belonged to its 3,707 labor unions.

b. The Right to Organize and Bargain Collectively: With the exception of civil servants, teachers, and defense industry workers, the Law Governing the Handling of Labor Disputes

(LUL), and the Collective Agreement Law give workers the right to organize and bargain collectively. However, the laws also restrict workers' exercise of these rights. The LUL, for example, stipulates that workers shall not strike to demand an increase in wages exceeding standard wages. Collective bargaining agreements exist mainly in large-scale enterprises. As of June, 1998, there were 296 such collective agreements.

c. Prohibition of Forced or Compulsory Labor: The Labor Standards Law prohibits forced or compulsory labor. The maximum jail sentence for violation of the law is five years. Except for cases involving prostitution, there were no reports of such practices in 1998.

d. Minimum Age for Employment of Children: The Labor Standards Law stipulates age 15, after completion of the 9-year compulsory education required by law, as the minimum age for employment. County and city labor bureaus enforce minimum age laws. Child labor is rare in Taiwan.

e. Acceptable Conditions of Work: The Labor Standards Law (LSL) mandates basic labor standards. Under a 1996 amendment, the LSL is to extend to all industries by the end of 1998. As a result, it now covers over 5.5 million of Taiwan's 6.6 million salaried workers. The minimum wage remained unchanged in 1998 at NT\$15,840 (or about \$490) per month. During 1998, the average wage in the manufacturing sector was around NT\$39,340 (or about \$1,320), more than twice the legal minimum wage. The LSL limits the workweek to 48 hours (8 hours per day, 6 days per week) and requires one day off every 7 days. In December 1996, the LSL was adjusted to give employers more flexibility in adhering to work hour limits and to facilitate the extension of a five-day workweek twice a month to private sector firms. In addition to wages, employers typically provide workers with additional payments and benefits, including a portion of national health insurance and labor insurance premiums, the distribution of labor welfare funds, meals, and transportation allowances.

f. Rights in Sectors with U.S. Investments: U.S. firms and joint ventures generally abide by Taiwan's labor law regulations. In terms of wages and other benefits, worker rights do not vary significantly by industrial sector.

**Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad
on an Historical Cost Basis -- 1997**

(Millions of U.S. Dollars)

Category	Amount
Petroleum	40
Total Manufacturing	3,193
Food & Kindred Products	96
Chemicals & Allied Products	1,350
Primary & Fabricated Metals	57
Industrial Machinery and Equipment	164
Electric & Electronic Equipment	1,023
Transportation Equipment	42
Other Manufacturing	462
Wholesale Trade	526
Banking	615
Finance/Insurance/Real Estate	288
Services	204
Other Industries	77
TOTAL ALL INDUSTRIES	4,944

Source: U.S. Department of Commerce, Bureau of Economic Analysis.